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Cato on implicit taxes of the individual mandate

Posted by [Don McCanne MD](#) on Thursday, Jan 14, 2010

This entry is from Dr. McCanne's Quote of the Day, a daily health policy update on the single-payer health care reform movement. The QotD is archived on PNHP's website.

Obama's Prescription for Low-Wage Workers: High Implicit Taxes, Higher Premiums

by **Michael F. Cannon**

Cato Institute

January 13, 2010

Executive Summary

House and Senate Democrats have produced health care legislation whose mandates, subsidies, tax penalties, and health insurance regulations would penalize work and reward Americans who refuse to purchase health insurance. As a result, the legislation could trap many Americans in low-wage jobs and cause even higher health-insurance premiums, government spending, and taxes than are envisioned in the legislation.

Those mandates and subsidies would impose effective marginal tax rates on low-wage workers that would average between 53 and 74 percent — and even reach as high as 82 percent — over broad ranges of earned income. By comparison, the wealthiest Americans would face tax rates no higher than 47.9 percent.

Over smaller ranges of earned income, the legislation would impose effective marginal tax rates that exceed 100 percent. Families of four would see effective marginal tax rates as high as 174 percent under the Senate bill and 159 percent under the House bill. Under the Senate bill, adults starting at \$14,560 who earn an additional \$560 would see their total income fall by \$200 due to higher taxes and reduced subsidies. Under the House bill, families of four starting at \$43,670 who earn an additional \$1,100 would see their total income fall by \$870.

In addition, middle-income workers could save as much as \$8,000 per year by dropping coverage and purchasing health insurance only when sick. Indeed, the legislation effectively removes any penalty on such behavior by forcing insurers to sell health insurance to the uninsured at standard premiums when they fall ill. The legislation would thus encourage “adverse selection” — an unstable situation that would drive insurance premiums, government spending, and taxes even higher.

<http://www.cato.org/pubs/pas/pa656.pdf>

Since the numbers and policy details in the final reform legislation have not yet been released, the results presented here by Michael Cannon of the Cato Institute may be modified, but unchanged will be the conclusion that the complex, jerry-rigged method of paying for health care premiums will not eliminate inequities.

It is almost impossible to get right the amount that each person or family should pay with so many variables moving in different directions: insurance premiums, actuarial values, premium subsidies, cost-sharing subsidies, income levels, family sizes, age rating, bracketed income cliffs of eligibility, and other factors. Financing health care by using a fixed premium for a given private insurance plan no longer works because premiums for adequate plans are no longer affordable for the majority. Trying to make health care affordable by applying corrections for the many variables increases the administrative complexity while falling short on equity.

Financing would be greatly simplified and much more equitable if we established a single risk pool that covered everyone and funded it through progressive taxes. (That likely would not be the conclusion of the libertarians at Cato, but they offered no alternative suggestions in this report, and we wouldn't agree with them anyway.)

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